KTS
CAPITAL
MANAGEMENT

KTS weekly update Nr. 47

The 24th of December 2021

More on Omicron and Covid19

- Moderna confirms that the Spikevax booster increases neutralizing antibody levels against Omicron by 37 fold. Higher doses increase even to 83 fold. This is a particular positive news, having had the company doubting the efficiency of the vaccine two weeks ago.
- Pfizer said that the US FDA had cleared the Covid-19 antiviral pill. That makes it the first at-home treatment for the coronavirus. The company also announced that it was ready to begin immediate delivery in the US and projected production of 120 million treatments in 2022.
- **We were also pleased to read in The New York Times, the magazine The Economist and CNBC (which for too long were only negative on the development of Omicron), that scientists in South Africa, Scotland, England and also US have found that Omicron infections more often result in mild illness than earlier variants of the coronavirus.** Apparently, the lowered risk of hospitalization in all three countries (in South Africa and UK 70-80% less likely to be hospitalized compared with other strains) appears to be due in large part to immunity in those populations, whether from vaccination or prior infection. In addition, more encouraging news came from South Africa, suggesting that the wave of infections may have already peaked.
- **We re-connect to the commentaries of Mr. Alessandro Fugnoli and Mr. Yardeni that Omicron is the the right opportunity to accelerate the pace towards achieving herd immunity.**
- Mr. US President Biden did not raise the subject of a new round of lockdowns during his speech about the pandemic. KTS is of the opinion that no government is in the financial position to do so.

Outlook Credit Suisse

- We attend multiple webinars and, as always, we like the arguments and outlook for 2022 from Credit Suisse's CIO, Mr. Dr. Burkhard Varnholt.
- We would like to highlight a few key points:
  - Basically, Credit Suisse is bullish on equity markets going forward and it is aligned with our best in class fund Flossbach & others. Both assert that company's earnings continue to grow, margins are improving and the global economy will still grow, although at a slower pace than in 2021.
  - During 2021, having experienced a tremendous increase in earnings, which were higher than analyst's estimations (fact also confirmed from Flossbach, Alkeon and Yardeni), equity markets increased less than earnings. This translated into a lower market P/E. Therefore, lower valuations and evidence that equity markets are definitely not in a bubble. On the contrary, equity markets are attractively valued and there is a good base for more upside potential during 2022.
  - Share buyback programs are going to increase further, which will provide strong support to equity markets.
  - The increase in labor wages should not be seen as a negative. As long as company's earnings are increasing it is fair to give a share to employees, especially in an inflationary environment, which was not the case in the last decade. Higher salaries is going to be translated into higher consumption, which finally means higher economic growth.

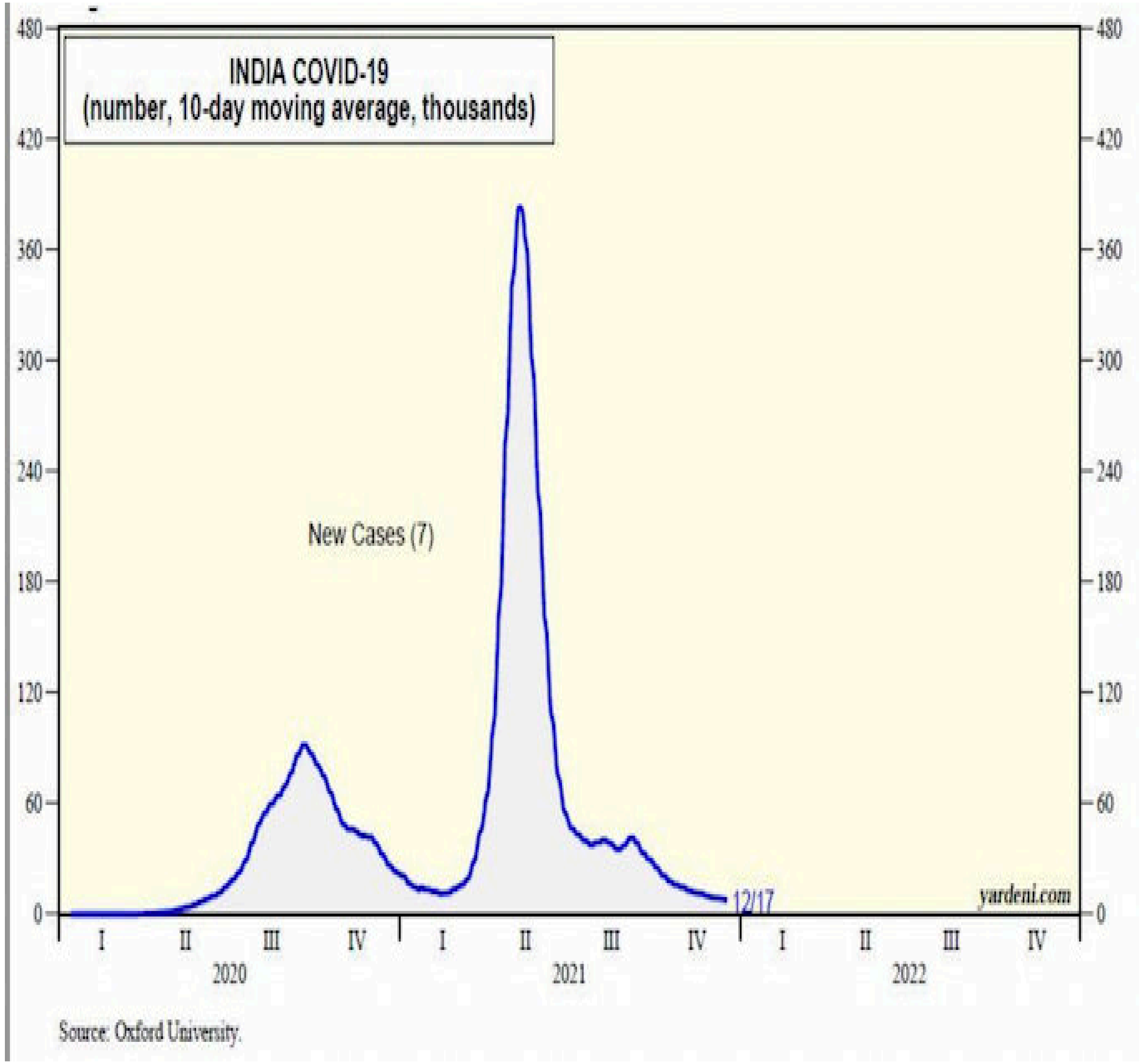
Outlook Credit Suisse

- Mr. Varnholt strongly believes we are in **one of the most important innovation decades in history.** There are many revolutionary technology trends emerging and he added that we have a **tsunami of innovation** and live in a 0% interest rate environment. **Venture capital structures are experiencing the best momentum in their history** with massive capital inflows, in addition to massive fiscal stimulus from governments. Mr. Varnholt also added that start ups are no longer “on their own”, like in the past. VC structures are not only deploying capital into the space, but now also bringing experience, know how and connections, helping to create a shorter path to success.
- We also liked their commentary on the inflation outlook, saying it should fall in the second half of 2022, because the components, which caused the inflation’s spike during 2021, are going to fall next year (energy, car and truck rental, used cars and trucks, hotel/lodging). Talking to companies, Credit Suisse also discovered that many are ordering more products than actually needed, with the hope of receiving the necessary quantity. This situation is going to, sometime in the future, produce the reverse effect, especially in the semiconductor sector. In addition, Mr. Varnholt is of the opinion that today`s situation is not comparable to 1970, but rather to 2013, 2015 and 2018.
- Credit Suisse is also of the opinion that no government or central bank will need to dramatically change the current accommodative monetary policy. Basically, also pointing out like Flossbach, that we are at the point of no return.
- Finally, also Credit Suisse is warning about possible **“black swans”**, which could potentially be the geopolitical tensions in **Ukraine and Taiwan, or increasing interest rates.** In the event equity markets do correct, it would actually present the opportunity to increase equity exposure, equity being the only really attractive asset class in today`s investment environment.

KTS feels comfortable with our our asset allocation, which happens to be in line with the Credit Suisse assessments.

Covid new cases in India

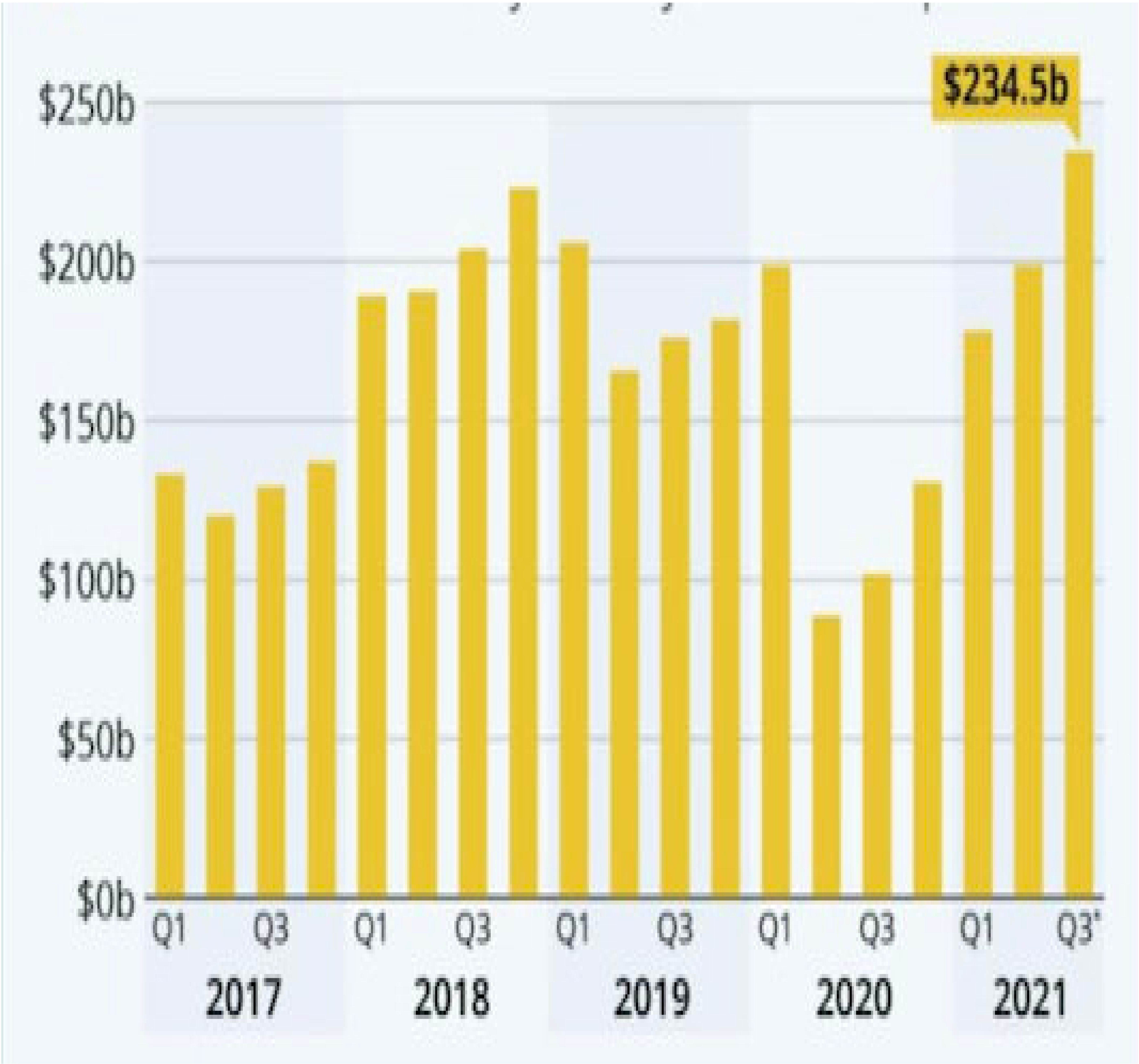
- We must admit that sometimes it sounds repetitive to mention market commentaries of the economist Mr. Edward Yardeni of Yardeni Research, but we are amazed, how he can “produce” the right arguments almost every time.
- This week, Mr. Yardeni is analyzing new daily Covid cases in India, which dropped from 401k in May to 7’400 today and, as he is rightly pointing out, **how is that possible despite the low double vaccination rate?**
- The logical answer is a **global natural immunity**, which may be more effective against the disease than the immunity provided by vaccinations! The real question now is what impact the Omicron variant will have on India. Taking into consideration that Omicron is 1/4 as lethal than Delta, we should be optimistic on the development.
- **According to research, 67.6% of people across India had Covid antibodies present**, providing them with a level of immunity against the virus. 24.8% have a single dose of vaccine and 13% were fully vaccinated.



India: daily new cases dropped from 401k to 7’400

Powerful share buyback programs: the natural hedge of equity markets

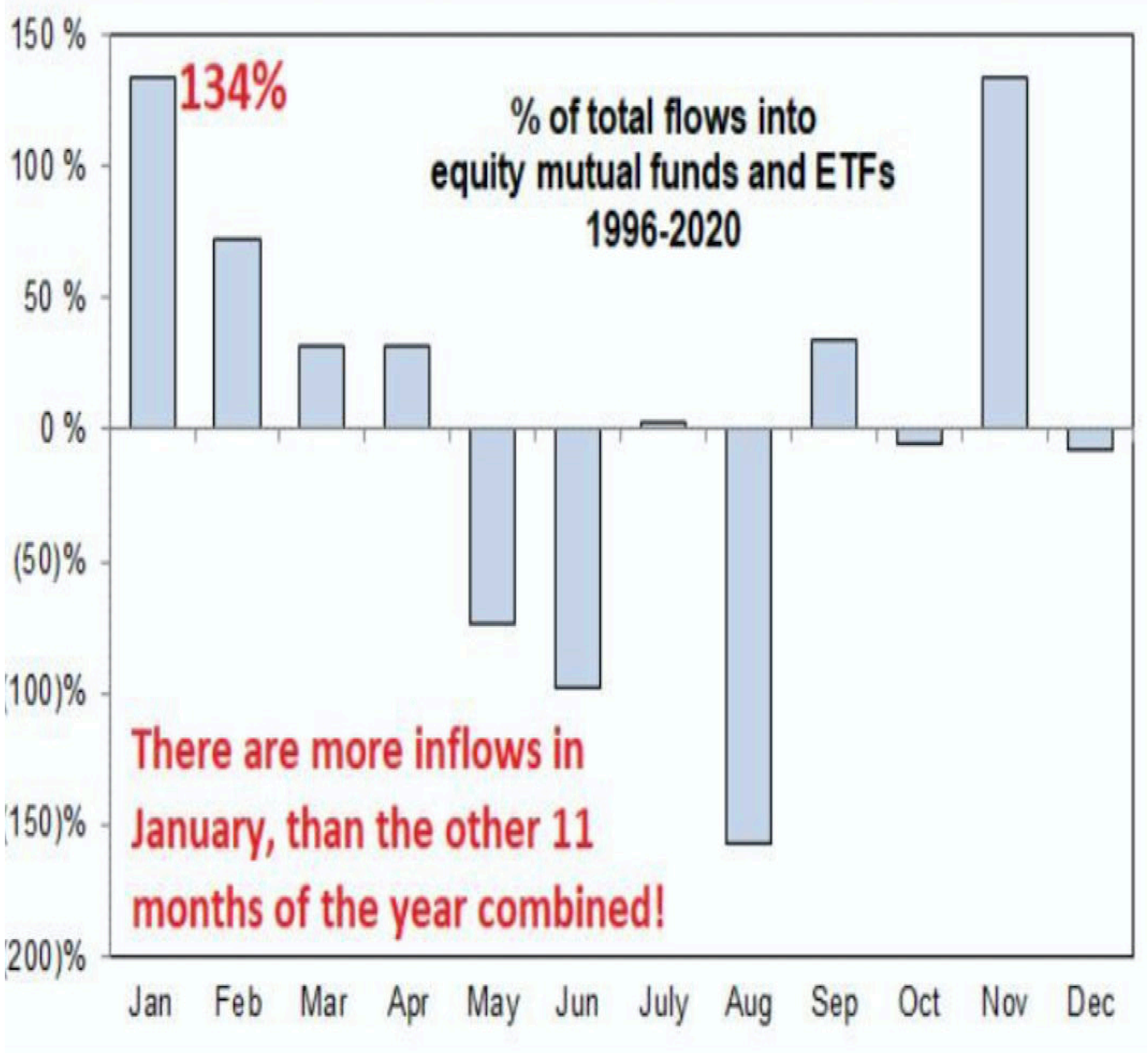
- S&P 500 Index buyback programs hit a new record with USD 234.5 billion in Q3 2021.
- About **53.8% of stock buyback activity in the US was fueled by the top 20 companies** and confirms KTS's theory that the outperformance of the majors was not only due to earning's growth and passive investments.
- Share buyback programs were reduced during the pandemic, but are running again at "full steam" and going forward the amount will most probably even increase.
- Extrapolating USD 235 billion a quarter, we could expect for 2022 a total amount of at least USD 940 billion to USD 1 trillion.
- This is a tremendous natural hedge for equity markets and in any market correction, companies going to "step in" with massive share buying programs, supporting equity markets and most probably avoiding any dramatic corrections, or definitely avoiding bear markets in the coming years.



S&P 500 Index buyback programs (source Statista / Bank Syz)

Equity inflows in January

- According to several statistics, during January of every year, equity markets experience the most important inflows, mostly because of pension plans forced to invest their "fresh" capital.
- The chart on our right, courtesy of Goldman Sachs (via Bank Syz), shows that January typically sees 134% of inflows and the rest of the 11 months is -34%.
- Goldman Sachs is arguing that taking into consideration that private wealth managers worldwide are increasing their allocation into equities, by selling bonds and reducing cash, we should expect additional flows of around USD 125 billion for January 2022 on top to company's share buy back programs.
- As we analyzed last week, most of professional asset managers are overweight cash. The CNN fear and greed index is at extreme fear levels, retail investor indicators are extremely bearish and December saw heavy volumes in tax selling. Some sector/stocks are at capitulation levels, so with such depressed market sentiment and very weak market breadth, we would expect a positive January for equity markets.



January inflows in equity markets the highest with +134%

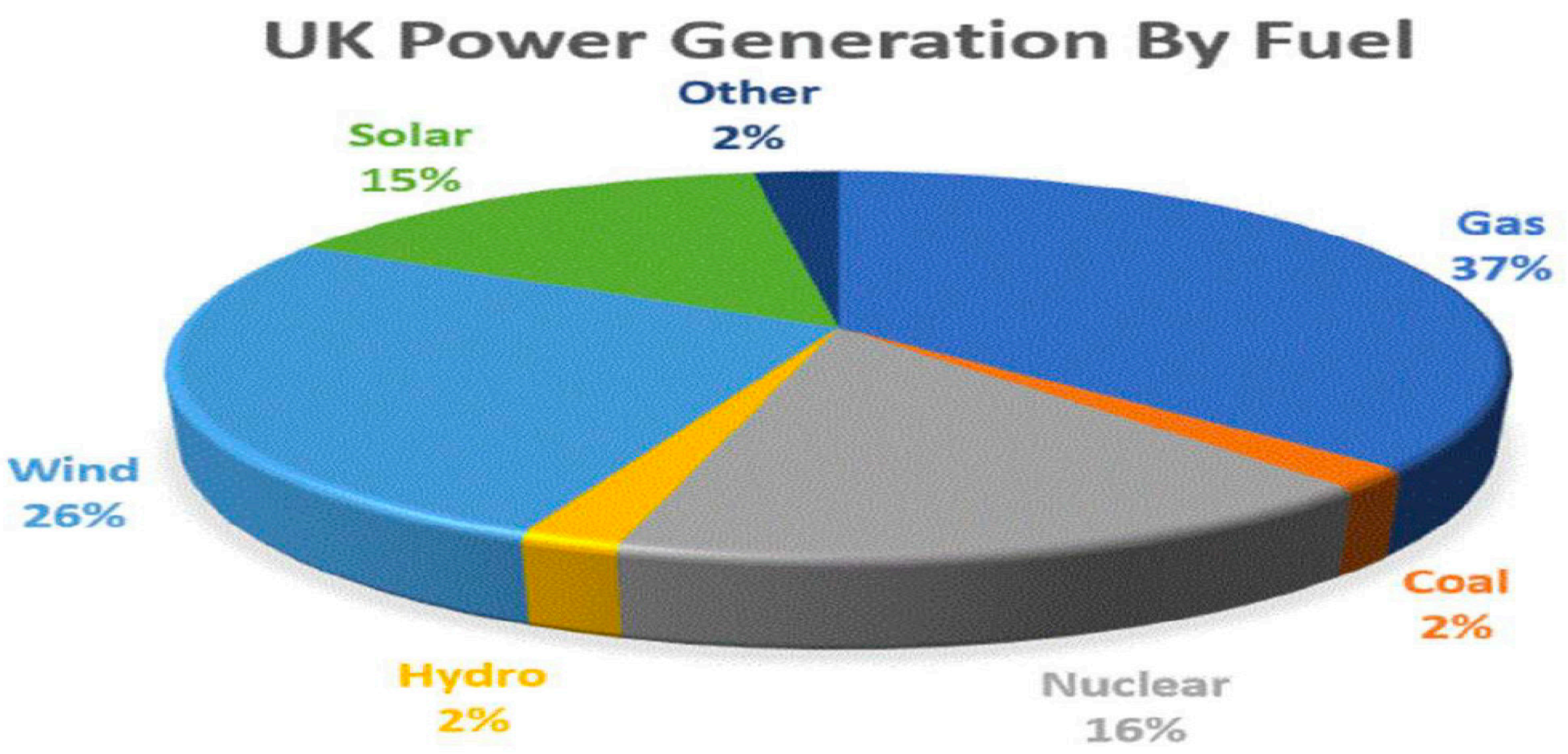
Value in the greening journey

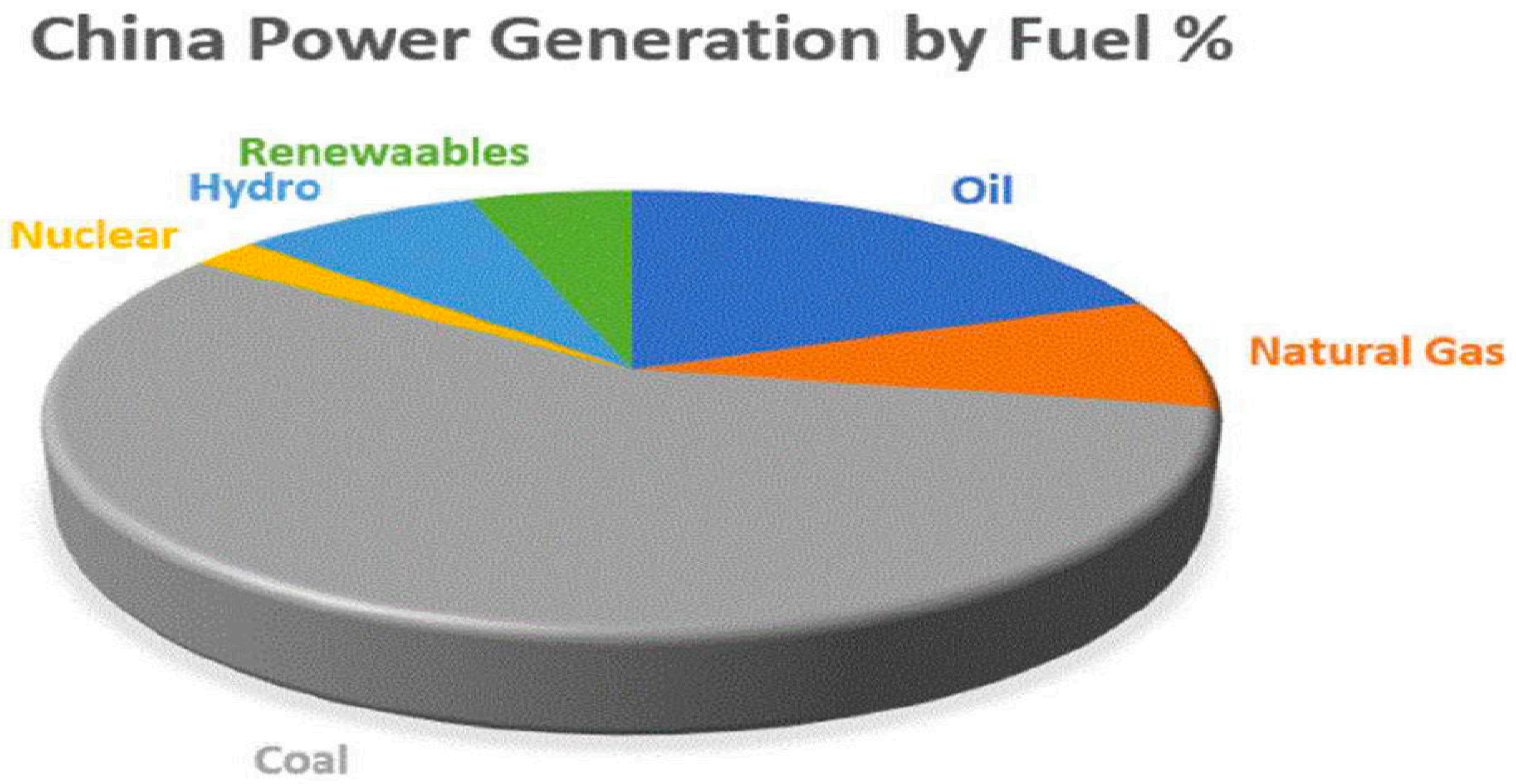
- As usual at the end of the year, we are having our round of discussions with our best in class fund managers in order to have a better long term picture and analyze our equity positioning for next year, in order to finalize our outlook and high convictions.
- Our expert for investments into sustainable and renewable assets re-enforces his opinion that in the coming years cheaply valued traditional fossil companies are going to experience multiple expansion due to improvement in ESG score.

Source Anaconda Invest

Diversification of UK power generation

- Our expert for renewable energy rightly points out that UK has better power generation diversification than, for example, China, which still has to intensify efforts to reduce coal power generation.
- By mapping the solar power by country in 2021, courtesy www.visualcapitalist.com, China is the leader with 254k MW and makes up 35.6% of the worldwide solar power, followed by US with 75k (10.6% worldwide), Japan 67k (9.4%), Germany 53k (7.5%), India 39k (5.5%), Italy 21k (3%). Australia has “only” 17k (2.5%) but the “small” Vietnam 16k (2.3%).
- We can see from such statistics that for China it is going to be very difficult to further diversify coal’s energy source with renewable (best example is the solar panel installation in Ruicheng County, central Shanxi province) and, therefore, comparing with UK the logical consequence is an increase into nuclear and gas. Therefore, our renewable energy **expert is focusing also into nuclear (example are smaller nuclear reactors in UK) , LNG, but also Wind**, which experienced a setback during the pandemic.





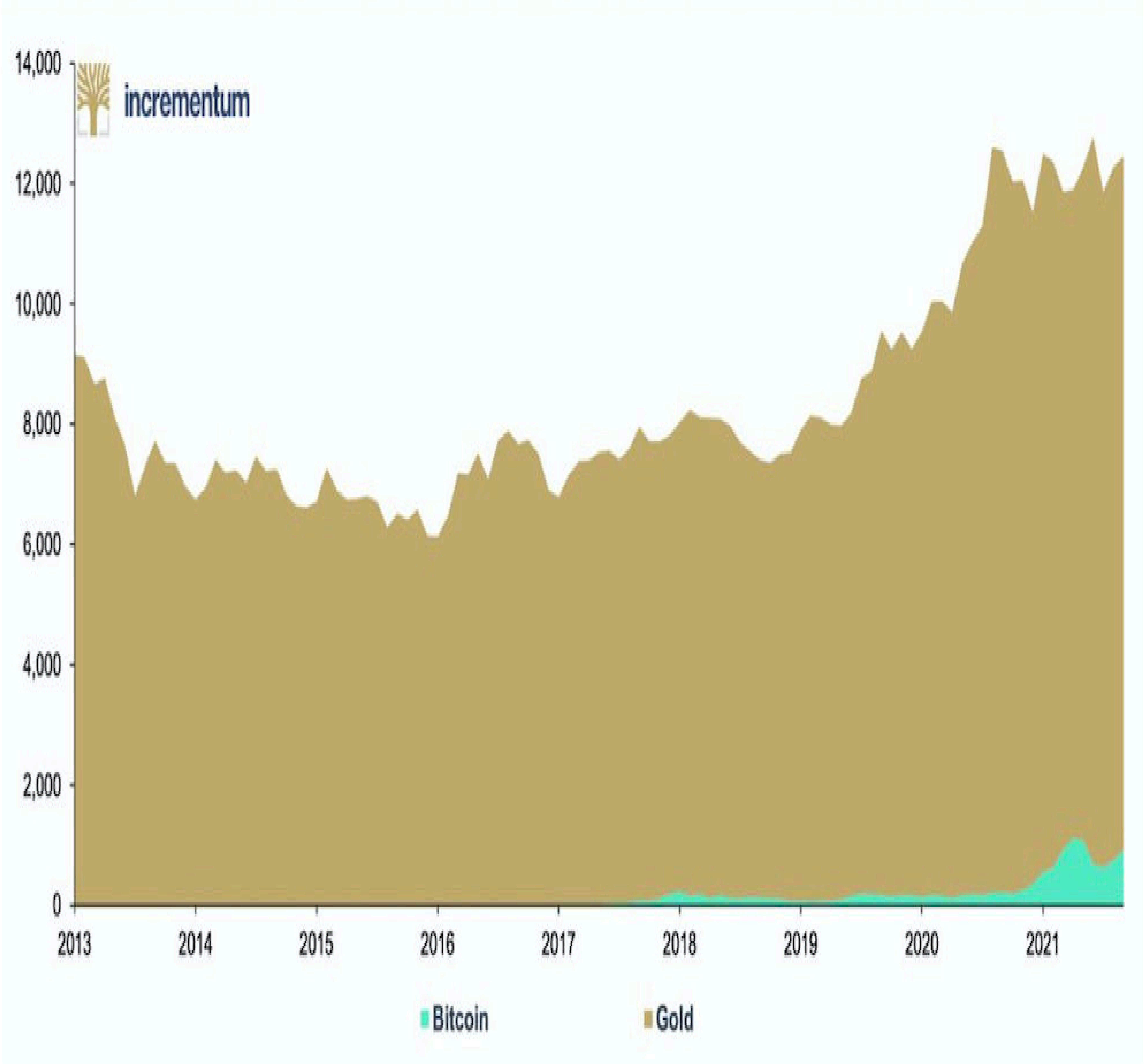
UK has a better power diversification diversification, for China is still a challenge (source: Anaconda Invest)

Precious metal sector

- According to Mr. Otavio Costa, nowadays just 5% of global equity markets include commodity producers and from those 5%, only 9% of investments flow into precious metals companies.
- Therefore, gold and silver stocks are the **ultimate deep-value opportunity.** We have known this to be the case since year 2020, but, of course, during year 2021 the performance of the sector was really poor. Even though gold miners steadily improved their margins, cash flows and dividends, which together translates into even more attractive valuations.
- We understand, the “music” is in the crypto space and all new crypto currency projects, especially into Metaverse or NTFs. Apart from the fact, as explained in the next slide, that volumes invested into cryptos would not have had a major impact on the gold price. We are actually now questioning the valuations in most of these new crypto trends. Therefore, we have kept our allocation of 5% in gold for our discretionary mandates, and we wait patiently because we believe the downside risk is quite limited, but the upside could be major. The potential is the contrary to many “phantasy” crypto projects or SPACs.
- Again, we also would like to re-mention the case of the Turkish Lira`s devaluation and the Argentine Peso. Citizens of those countries, who were invested in gold, could avoid the dramatic loss in the purchasing power of their cash. This reality shows once again the importance of long term diversification in the portfolio, especially for citizens in emerging markets. Also, we have not to forget that main currencies like USD, EUR and JPY do not have strong fundamentals either. In addition, investors feeling safe holding Swiss Francs should worry about the huge currency balance sheet, especially he EUR, of the Swiss National Bank. Therefore, gold is almost an unique safe heaven worldwide.

Market capitalization of Bitcoin vs Gold

- The chart on the right, courtesy of Incrementum (via Mr. Mattia Cremonini), shows that the total market cap of bitcoin is USD 1 trillion vs USD 13 trillion for gold.
- Therefore, even though during 2021 the “real music” was indeed into crypto currencies, it was in such “small” volume, compared to the global gold market, that it was insignificant. The conclusion is that the gold’s weakness cannot be explained with the inflows into crypto currencies.
- In fact, if the whole inflows into cryptos (around USD 500 billion for 2021) had been invested into gold, it would have caused an impact of “only” around 5% of the global gold’s market.



Source: Incrementum / Mattia Cremonini

Turkish Lira devaluation

- The Turkish president Mr. Erdogan tricks to save the Turkish Lira by basically promising the Turkish government to reimburse retail people of all mark to market losses in any currencies against the Turkish Lira, if those losses would exceed the interest rate they can gain by owning deposits in TRY rather than switching to another currency.
- Without to go to deep into detail of FX mechanisms, basically a Turkish retail would have today a free carry in TRY vs any foreign currency. The first natural reaction of the KTS team was, can the Turkish government afford such intervention? The reaction of the TRY vs USD was amazing: +40% from the intraday lows. Most commentaries in the net are just wondering if the intervention could succeed on the long term.
- We would like to mention the commentary of Mr. Alfonso Peccatiello, who is rightly questioning, that the risk is moved from the Turkish private sector to the government balance sheet, but who is going to backstop that? The conclusion is, **Mr. Erdogan is playing out a psychological move with the hope**, Turkish retails are going to stop switching into USD, Gold or EUR and try to calm down flows. Most probably, Mr. Erdogan can slow down the trend, but not stop it and the **Turkish government can offset additional losses only by printing more money, which is translated in higher devaluation over longer term.**
- If we analyze the trend of the Argentine Peso, investors should realize, on the longer term there is only one trend and it is negative. KTS was monitoring the Turkish Lira development with the intention to possibly invest into an EIB bond in TRY, but the situation is definitely to unstable and therefore we decided to cancel such investment from our radar screen.
- As explained multiple times this year, for Turkish citizens, to be invested in gold was a perfect hedge against inflation and the huge devaluation of the Turkish Lira (over 50%). The same apply also for Argentinian, South African and Brazilian citizens.

Special situation Nevada Copper

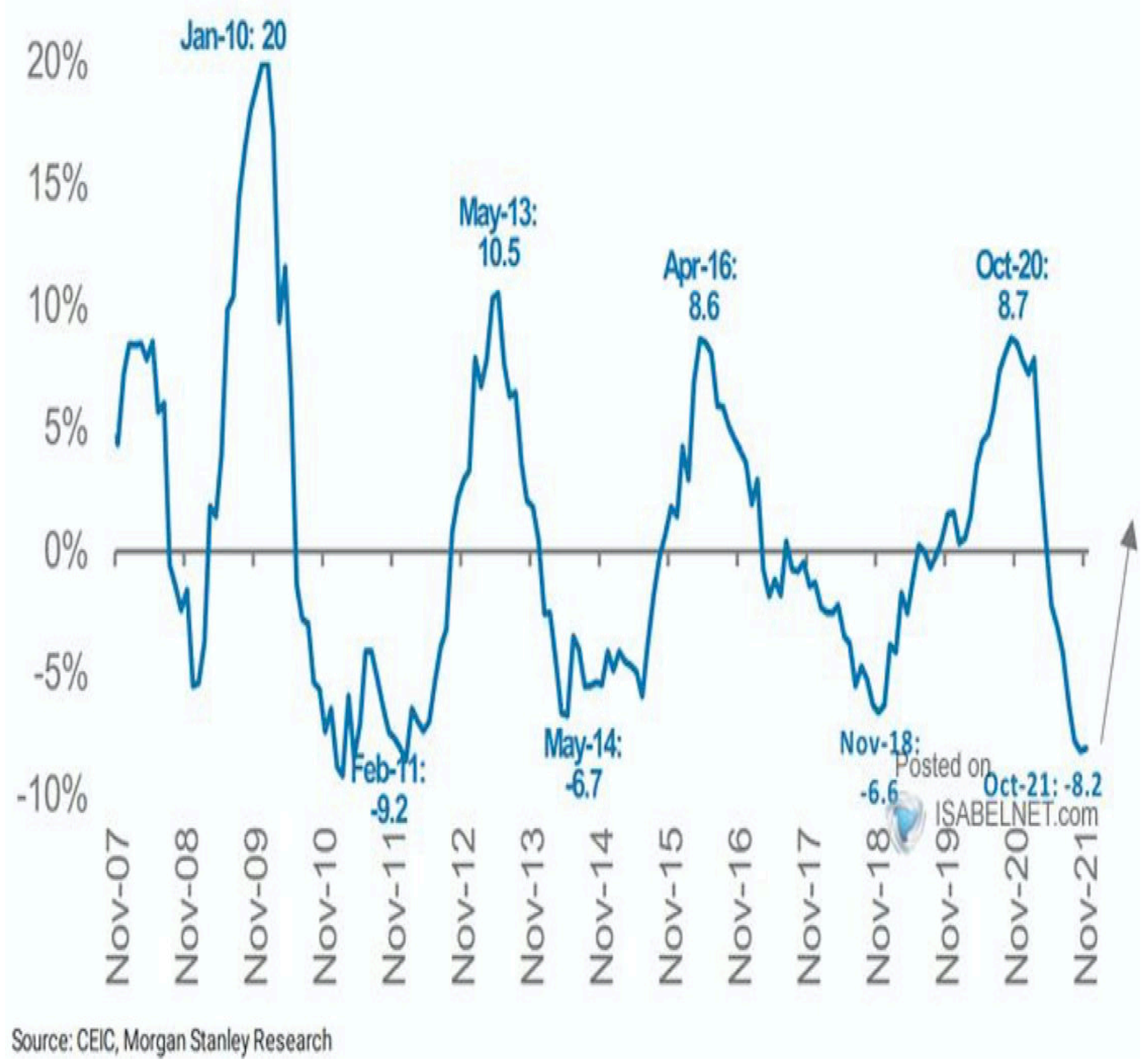
- We would like to analyze again the investment case, after the main investors recently injected around USD 115 mio in an oversubscribed placement at 0.77 CAD. But the stock is now trading lower, a fact that does not make any real sense. The actual market price can only be explained by substantial US tax selling and that the three majors shareholders are not focused on the short term, rather on the long term. Even so, such an answer cannot explain satisfactorily why the placement was oversubscribed at 0.77 CAD and yet there is no real buyer interested at around 0.60 CAD?
- KTS is keeping the fundamentals in focus and we would like to mention that Nevada Copper is a junior miner, which should finally get into production after several issues, mainly due to the Covid19 pandemic. It is the **only junior miner with a permitted open pit in developed markets.**
- We all know copper is heavily undersupplied and the world will need substantial more supply of copper going forward, due to the "green" transition and massive infrastructure stimulus packages. Therefore, major copper producers, which held back new investments because of increasing ESG regulations, will be forced to acquire new projects, sooner rather than later, in order to satisfy higher demand. When major copper producers analyze possible M&A candidates, the priority going to be into countries with political stability and existing permitted projects, therefore they hardly can pass over Nevada Copper.
- Nevada Copper can count on strong shareholders like Pala Investment, Mercuria and Solway, which are basically holding more than 60% of the outstanding shares with a total investment of well over the actual market cap of around CAD 300 mio.
- We could also understand, that a major shareholder, Castlelake, had to liquidate the whole position (over 15%) due to internal restructuring and focusing again only on the core business.

Special situation Nevada Copper

- In a recent interview, the new CEO of the company, Mr. Randy Buffington, confirmed the increase and improvement of production and claimed the worst was now behind them. The company has over USD 68mio in cash and a USD 130mio senior debt facility from KfW development Bank. And added that, if not so already, during Q4 2021 will be cash flow positive.
- Finally, the real trigger going forward is the extension drilling and potentially a feasibility study of the open pit mine.
- The non-executive chair, Stephen Gil, adding to an interview said that the pit shell needs to be optimized for the current copper price. The existing pit shell production cost is at USD 2.45 per pound copper, against a market price is at USD 4. Forecasts are for even higher prices in the future. For this reason there is tremendous upside potential in the valuation.
- In fact, a higher copper price encourages the company to look at the open pit as a single 70’000 tpd (tons per day) development, rather than a phased approach. The company can add about 50% to the net present value (NPV) of the project through the low-hanging fruit.
- The company is also improving its ESG score by planning solar power (200MW capacity, sufficient for the needs of the open pit), autonomous fleet (for the open pit) or electric trucks for the underground mine.
- In addition, the company Nevada Copper is also starting to look at the broader potential of its land package beyond the underground and open pit scenarios, adding further upside potential to the NPV.
- We increased our exposure during the recent correction and we wait patiently for the huge upside potential. Once again, of course, we must not fall in love with a stock. However, the sum of parts valuation, the fundamentals of the copper sector, the “green” transition and the strong backup from industrial shareholders give us confidence, that we will be positively surprised.

News on China

- As we all know, China is constantly reducing its exposure to US T-Bills, instead it is diversifying worldwide. In fact, **China lent about USD 1.5 trillion in direct loans and trade credits to more than 150 countries around the globe.** Therefore, China nowadays is the **largest official creditor,** surpassing traditional, official lenders such as the World Bank, the IMF, or all OECD creditor governments combined!
- On the chart on the right, courtesy Mr. Ansidei / MS research, we can see how the Chinese credit impulse is expected to rise and this should strongly support the Chinese economy.



CHINA'S CREDIT IMPULSE % OF GDP (source: MS via Mr. Ansidei)

General news on cryptos

- The crypto space **attracted more money in 2021 than all previous years combined.** Apparently, venture capital funds have poured about USD 30 billion into crypto, almost quadruple the amount spent at the previous peak of around USD 8 billion in 2018. Investments went across the whole spectrum, from financial services, to art, gaming, NFTs, Web 3.0, decentralized social media, play-to-earn, etc.
- Analyzing valuation and volume in the space, it sounds more like a bubble. We are not questioning the technology, which is undoubtedly the base for the future in the finance sector, but what is definitely questionable is the price paid for certain NTFs or the valuation of many start ups in the sector.
- **The highest sales of Christie`s during 2021 compared to the past is strongly correlated with NFTs and millennials: in fact, Christie`s confirms that 1/3 of its bidders this year were first-timers to the company and 1/3 of those newcomers were millennials.**
- We have to admit, we are aware of Metaverse realities like Sandbox and we realized, there is a lot of “actions” in the segment, especially reading recently that even PwC Hong Kong is acquiring a plot of LAND in The Sandbox (virtual real estate represented as a non-fungible token - NFT) for USD 10k as a part of an experiment to explore forward-thinking business. We also understand that many NFTs are already connected to ticketing, music, etc in the “real world” and therefore have a practical use, but the knowledge of KTS is still too sporadically in order to give an opinion. We are keeping an intensive discussion with experts in the field, having read that the global search interest for “NFT” surpasses “crypto” for the first time ever lately and therefore the space is gaining traction, especially by younger generations.

General news on cryptos

- The Chinese tech giant Baidu says it could be 6 years before it can fully deliver its Metaverse. With such news we all can understand, that the trend is clear, but it will take sometime, before Metaverse going to be our daily reality and therefore the “rush” especially at insane valuations, could turn out to be the same at the “tech bubble” in year 2000, where the technology was the right one, but just too early.

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